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IN THE

SUPREME COURT OF THE UNITED STATES.

OCTOBER TERM, 1944.

P. D. GEORGE,
Petitioner,

v.

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

No. 595

PETITION FOR WRIT OF CERTIORARI

To the United States Circuit Court of Appeals for the Eighth Circuit,

and

BRIEF IN SUPPORT.

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P. D. GEORGE,
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COMMISSIONER OF INTERNAL REVENUE,
Respondent.

No. .....

PETITION FOR WRIT OF CERTIORARI

To the United States Circuit Court of Appeals for the Eighth Circuit.

To the Honorable Supreme Court of the United States:

The petitioner, P. D. George, respectfully prays that a Writ of Certiorari issue to review the judgment of the United States Circuit Court of Appeals for the Eighth Circuit in cause styled: "P. D. George, Petitioner, v. Commissioner of Internal Revenue, Respondent," affirming the decision of The Tax Court of the United States.

JUDGMENT AND APPLICATION FOR CERTIORARI.

The judgment of the United States Circuit Court of Appeals was entered on July 17, 1944 (R. p. 54), and this petition is filed within three months thereafter.

STATEMENT OF THE CASE.

On December 23, 1939, petitioner created a trust, naming himself and two other individuals, Fred S. Henderson and Joseph S. Malecek, as trustees. Neither Henderson nor Malecek is related to petitioner (R. pp. 11, 30, 32). Petitioner transferred to the trustees 640 shares of capital stock of the P. D. George Company, a Delaware corporation.

Prior to the creation of said trust, the petitioner owned all of the 1,000 shares of the P. D. George Company stock. In addition to the transfer of the 640 shares to the trust for the benefit of his sons, the petitioner, about the same time, transferred 60 shares of such stock by direct gift to six of his sons (R. p. 31).

The trust instrument provided, inter alia, that the assets thereof were to be divided into seven parts. The income of the first of such parts was to be paid to grantor's son, Pericles F. George, in quarterly or other convenient installments for life, or in certain eventualities to his wife and children, and on his death the corpus was to be distributed to his then living children and to the descendants of any child then dead, per stirpes. The entire net income of the remaining six parts was to be paid to the six other sons equally in quarterly or other convenient installments until five years after the death of the petitioner, at which time the corpus of those parts, then remaining, was to be distributed to the six sons or, in the event of the death of any of them before the period of termination, to his descendants, per stirpes (R. pp. 34, 35).

The trust is irrevocable. **The grantor could not make any amendment or change by which any of the income could become payable to him or for his benefit, or held or accumulated for him, or any of the principal could be paid to him or for his use or benefit.** Under Article Six of the trust instrument, the grantor reserved the right (subject to the limitation mentioned) upon notice (1) to substitute other beneficiaries in place of those named; (2) to add to

the number of the beneficiaries and to direct the distribution of income or principal otherwise than as provided in the trust instrument; (3) to alter or cancel the amount of income or principal to be distributed to or applied to the use of any of the beneficiaries; (4) to direct distribution of any share to a beneficiary who might then be entitled to the current income (R. pp. 36, 37).

The reserved powers of the grantor could be exercised only by instrument signed by him and delivered to the trustees, but (1) no change or amendment **became effective until thirty days** after such instrument was delivered, (2) the amendment applied only to income derived **after** the amendment became effective, that is, the right of the beneficiaries to income derived before the amendment became effective could not be taken away from them (R. p. 37).

The petitioner has never exercised any of his said powers (R. p. 13).

When the trust agreement was executed (1939), the youngest of the petitioner's sons was twenty-nine years of age and the oldest was forty-three years of age. For many years prior to 1939, and continuously since, the seven sons have been married and living apart from the petitioner and apart from each other. During 1939 and for many years prior thereto, each of the seven sons had an independent income, in addition to his share in 1939 of the trust income, and maintained himself and his family (R. pp. 13, 14).

The income of the trust involved in this controversy covering the year 1939 was all received by the trustees within thirty days after the trust was created. All of the net income of the trust so received was distributed to the named beneficiaries (R. p. 31).

The Tax Court held that all of the net income of the trust estate was includable in petitioner's income for the year 1939 (R. pp. 10-24).

On appeal, the United States Circuit Court of Appeals for the Eighth Circuit, in opinion entered July 17, 1944, affirmed the decision of The Tax Court (R. p. 54).

JURISDICTION.

The jurisdiction of this Court is invoked under Section 240 of the Judicial Code as amended by the Act of February 13, 1925, Chapter 229, 43 Stat. 939, 28 U. S. C. A. 347. *Helvering v. Clifford*, 309 U. S. 331; *Helvering v. Stuart*, 317 U. S. 154.

STATUTE INVOLVED.

The Federal statute involved is Section 22 (a) of the Internal Revenue Code and is as follows:

> "Section 22. Gross Income.
>
> "(a) **General Definition.**—'Gross income' includes gains, profits, and income derived from salaries, wages, or compensation for personal service (including personal service as an officer or employee of a State, or any political subdivision thereof, or any agency or instrumentality of any one or more of the foregoing), of whatever kind and in whatever form paid, or from professions, vocations, trades, businesses, commerce, or sales, or dealings in property, whether real or personal, growing out of the ownership or use of or interest in such property; also from interest, rent, dividends, securities, or the transaction of any business carried on for gain or profit, or gains or profits and income derived from any source whatever. In the case of Presidents of the United States and judges of courts of the United States taking office after June 6, 1932, the compensation received as such shall be included in gross income; and all Acts fixing the compensation of such Presidents and Judges are hereby amended accordingly. In the case of judges of courts of the United States who took office on or before June 6, 1932, the compensation received as such shall be included in gross income."

DECISION OF LOWER COURT.

The Circuit Court of Appeals decided that petitioner remained the substantial owner of the trust property because he retained power to substitute beneficiaries, add to the number of beneficiaries, and direct current distribution of the trust property to the then income beneficiaries. Petitioner did not control the trustees and did not control the administration of the trust property and could not use any power in such manner as to derive for himself any economic benefit from the corpus or income, and his power did not extend to the income in controversy.

QUESTION PRESENTED.

Whether the grantor of an irrevocable trust enduring for his life, who has retained the power to change beneficiaries and accelerate the distribution of the corpus to the beneficiaries of the trust but may not benefit economically through any power, remains owner of the trust property so that all the income is his and taxable to him under Section 22 (a) of the Internal Revenue Code; notwithstanding (1) that he has parted with the power to administer or control the administration of the trust and (2) that the grantor is without any dependent, so that there is no intimate member of his family for whose benefit he could use his power, and (3) (subsidiary thereto) his power was so limited that it did not extend and never could have extended to the income involved in the controversy.

REASONS FOR ALLOWANCE OF THE WRIT.

I.

(A) The Circuit Court of Appeals has decided an important question in conflict with the applicable decisions of this Court. The question is whether the right of a grantor in trust to appoint the use of the trust property

to others than himself (with no other rights as to the trust property or income) is equivalent to ownership.

In *Helvering v. Clifford*, 309 U. S. 331, the Court held that the grantor of that trust retained all of the rights of an owner and therefore the trust was without substance. **None of the criteria of ownership found in the Clifford case exist in this case** (*Pearce v. Commissioner*, 315 U. S. 553). "Economic gain realized or realizable by the taxpayer is necessary to produce a taxable income under our statutory scheme" (*Helvering v. Stuart*, 317 U. S. 154).

Petitioner could derive no economic gain from his power to change beneficiaries (*John Stuart*, 2 T. C. 1103).

(B) The decision in this case is in conflict with the decisions of the Second Circuit in *Knapp v. Hoey*, 104 F. (2d) 99, and in *Commissioner v. Buck*, 120 F. (2d) 775, and the decision of the First Circuit in *Commissioner v. Bateman*, 127 F. (2d) 266.

No other Court of Appeals has held a retained power to change the beneficiaries **alone** (where the beneficiaries were not intimate members of grantor's family and the grantor did not possess, individually or as trustee or through control of the trustees, power to control administration of the corpus) made the grantor, after his irrevocable transfer to the trustees, the owner of the corpus and taxable on its income. A power of appointment of trust property retained by the grantor does "not amount to an estate or interest in the property." His interest is the same as that of a donee of a power (*Porter v. Commissioner*, 288 U. S., l. c. 441; *Commissioner v. Bateman*, supra).

(C) The decision in this case is in conflict with the decisions of the Second Circuit in *Commissioner v. Jonas*, 122 F. (2d) 169; the Third Circuit in *Helvering v. Bok*, 132 Fed. (2d) 365; the Tax Court in *Dunlevy-Milbank*, 41 B. T. A. 1014; the Tenth Circuit in *Jones v. Norris*, 122 F. (2d) 6; and the Sixth Circuit in *Central National Bank*

of Cleveland v. Commissioner, 141 F. (2d) 352. The power of grantor did not extend to the income involved in this case or to the interest in the corpus out of which such income arose. It was an unalterable trust during that short period, and there was no reversion in the grantor.

II.

This Court should take jurisdiction of this case for the further reason that it alone can clarify its position. The Treasury's interpretation of the decision in the *Clifford* case, sustained by many of the lower courts, has destroyed the statutory code, formerly the guidance. Congress, taxpayers, and the lower courts have no guidance,—a corrosive situation under national **taxation**, particularly when the rates are so high.

Congress cannot act with discretion, because it cannot discover the governing criteria. Examples are Section 134 of the 1943 Revenue Act, which is in conflict with the law as stated in the Court of Appeals' decision in this case; and Section 111 of the 1942 Act, amending Section 22 (b) (3), which undermines its basis and is destructive of the fabric of the law. Only this Court can solve this snarl.

Wherefore, your petitioner respectfully prays that a Writ of Certiorari be issued out of and under the seal of this Honorable Court, directed to the United States Circuit Court of Appeals, Eighth Circuit, commanding that court to certify and to send to this Court for its review and determination, on a day certain to be therein named, a full and complete transcript of the record and all proceedings in the case numbered and entitled on its docket, No. 12,783, P. D. George, Petitioner, v. Commissioner of Internal Revenue, Respondent, and that the said judgment of the United States Circuit Court of Appeals may be reversed by this Honorable Court, and that your petitioner

may have such other and further relief in the premises as to this Honorable Court may seem meet and just; and your petitioner will ever pray.

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No. .....

BRIEF IN SUPPORT OF PETITION FOR WRIT OF CERTIORARI.

OPINION BELOW.

The opinion of the United States Circuit Court of Appeals, Eighth Circuit, is reported under the title "P. D. George v. Commissioner of Internal Revenue," 143 F. (2d) 837 to 842, and is printed on pages 44 to 53 of the Record.

JURISDICTION.

The judgment of the Court of Appeals for review was entered July 17, 1944 (R. 54).

This is a civil suit originated by petition to The Tax Court of the United States to review a deficiency in income taxes determined by the Commissioner of Internal Revenue

and upon petition by the taxpayer from an adverse judgment of The Tax Court reviewed by the United States Circuit Court of Appeals for the Eighth Circuit. The Writ of Certiorari is sought, directed to the United States Circuit Court of Appeals for the Eighth Circuit. The jurisdiction of this Court is invoked under Section 240 (a) of the Judicial Code as amended by the Act of February 13, 1925 (Title 28, U. S. C. A., Sec. 346).

STATEMENT OF FACTS.

A full statement of the facts is given in the petition for the Writ of Certiorari under heading "Statement of the Case." For the sake of brevity it is not repeated here.

SPECIFICATION OF ERRORS.

The decision of the Court of Appeals is erroneous and is contrary to the decisions of the other Federal courts in the following finding and ruling:

That petitioner, grantor of the trust, was the owner of the trust property, so that under Section 22 (a), Revenue Act of 1938, he was taxable upon the trust income for 1939 (which was distributable to the beneficiaries named in the trust, without any power in petitioner to deprive them of it), **merely** because petitioner retained the power to change the beneficiaries of the corpus and of income derived by the trust after the year in question, and notwithstanding that no beneficiary is an intimate member of petitioner's family and also that neither individually nor as trustee could he control the administration of the trust.

SUMMARY OF THE ARGUMENT.

1. **The income of an irrevocable trust is not taxable to the settlor because of his retention of the mere power to change the beneficiaries of the property and of the income if the grantor may not be a beneficiary.** This power, relatively inconsiderable, is not equivalent to ownership of the trust property so as to attribute its income to him.

Helvering v. Horst, 311 U. S. 112, and subsequent decisions, ruling that power to dispose of **income** from property owned is equivalent to the receipt of such **income** are not applicable. That ruling is based upon the principle, that delivery is essential to a gift, that income prior to its receipt, actually or constructively, is not in being and cannot be delivered, therefore the power to give is conditioned upon receipt.

> Rose v. Commissioner, 65 F. (2d) 616;
> Pearce v. Commissioner, 315 U. S. 543;
> Helvering v. Stuart, 317 U. S. 154.

The ruling in the *Horst* case that the power to give income from property **owned by the taxpayer** is equivalent to the receipt of such income, is taken by the Court of Appeals in this case to require the conclusion that the power to give income from property **not so owned** is equivalent to ownership of the property. That is an inappropriate and illogical conclusion.

The decisions of this Court in gift tax cases that when the grantor of a trust retains a power to change beneficiaries a gift is not complete, are not in point because in such cases the beneficiaries of a trust are the donees (*Helvering v. Hutchings,* 312 U. S. 393), and if the grantor retains the power to make a gift he cannot have already made a gift—the taxable act.

The trust was real. Petitioner dispossessed himself of all title. His single power was not equivalent to the ownership of the property.

> Commissioner v. Buck, 120 F. (2d) 775;
> Helvering v. Stuart, supra;
> John Stuart, 2 T. C. 1103.

The decision of the Court is contrary to Sections 161 to 167, Internal Revenue Code. Sections 161 to 165 lay down the general rule for the taxation of trust income. Sections 166 and 167, exceptions to this general rule, make the trust income taxable to the grantor where the trust is subject to the conditions stated in these sections. The detailed and accurate exclusion from Sections 166 and 167 of any trust, where the grantor can receive no economic benefit from the trust income or corpus, exclude from taxation in that manner income of trusts such as this, under which the grantor may receive no economic benefit.

The Clifford case properly construed, means only this: Trust income not payable to the settlor is nevertheless taxable to him when the trust is not real and without substance.

2. **The decision of the Court in the case at bar is directly in conflict with the decisions of other Circuit Courts of Appeal.**

> Knapp v. Hoey, 104 F. (2d) 99;
> Commissioner v. Bateman, 127 F. (2d) 266.

3. **The power of the settlor did not exist during the period when the income in question was derived and could never affect the right to such income.**

This trust was an irrevocable, unchangeable and unalterable trust for thirty days after its creation, and it was during this period that the income in question was

derived. It was an unchangeable short-term trust for that period. Considering that there was no reversion after that period, it is ruled by those decisions holding short-term trusts valid.

Commissioner v. Bok, 132 F. (2d) 365;
Commissioner v. Jonas, 122 F. (2d) 169;
Jones v. Norris, 122 F. (2d) 6;
Central National Bank of Cleveland v. Commissioner, 141 F. (2d) 352;
Dunlevy-Milbank, 41 B. T. A. 1014.

4. The end result of the conflicting constructions of this Court's decision in the Clifford case has been intolerable confusion.

The lower courts, construing the *Clifford* case, have found conflicting governing criteria, to wit:

(a) Retained administrative power.

Stockstrom v. Commissioner, 3 T. C. 255;
United States v. Anderson, 132 F. (2d) 98.

Contra:

Commissioner v. Katz, 139 F. (2d) 107;
Plimpton v. Commissioner, 135 F. (2d) 482.

(b) Retained power to change beneficiaries if coupled with distribution in intimate family group and administrative control.

Commissioner v. Buck, 120 F. (2d) 775.

Contra:

George v. Commissioner (the case at bar, in which there was such retained power without any such additional facts).

(c) The short-term of the trust.

Price v. Commissioner, 132 F. (2d) 95.

Contra:

See cases, supra, Point 3.

The Tax Court and the Courts of Appeal are all uncertain.

Commissioner v. Katz, supra;
Suhr v. Commissioner, 126 F. (2d) 283;
Armstrong v. Commissioner, 143 F. (2d) 700;
Harvard Law Review, July, 1944, page 884, note 368.

Congress is also confused.

Sec. 111, Revenue Act of 1942, amending Sec. 22 (b) (3), I. R. C.;
Irwin v. Gavit, 268 U. S. 161;
Sec. 134, Revenue Act of 1943, enacted Feb. 25, 1944;
Williamson v. Commissioner, 132 F. (2d) 489.

ARGUMENT.

I.

The Income of an Irrevocable Trust Is Not Taxable to the Settlor Because of His Retention of the Mere Power to Change the Beneficiaries of the Property and of the Income if the Grantor May Not Be a Beneficiary. Such Power Is Not Equivalent to Ownership of the Trust Property.

In *Helvering v. Horst*, 311 U. S. 112, relied upon by the Court of Appeals, this Court said:

> "The power to dispose of income is the equivalent of ownership of it. The exercise of that power to procure the payment of income to another is the enjoyment and hence the realization of the income by him who exercises it."

This or a similar statement has been made in other cases hereafter mentioned. But this statement must be read in its context. It was true under the facts of those cases. **It is not a general rule applicable to every case.** In all the cases where this statement is made, there was no question of the ownership of the property producing the income. Notice this Court did not say the power to dispose of **property** is the equivalent of ownership of the **property**.

In the *Horst* case, supra, the donor was the owner of the bonds from which he clipped and gave away the coupons. The interest, represented by the coupons, was, in the words of the court, "that which he could have received himself." In *Harrison v. Schaffner*, 312 U. S. 579, the donor, beneficiary of the trust, was the owner of the equitable interest in the trust property and could have received the income which she gave away. In *Helvering v. Eubank*, 311 U. S. 122, the assignor of the renewal

insurance commissions was the owner of the contract out of which such commissions arose and had the right to receive the commissions.

The Owner of Property Does Not Have the Power to Make a Gift of the Income Therefrom Without First Receiving Such Income.

Ability **of the owner of property** to give income away is equivalent to the enjoyment and realization of the income arising therefrom, **because it is legally conditioned upon the prior receipt of such income** for the following reason:

Income, as the word implies, is something coming in. It is derived from capital or from labor or from both combined. Capital is the tree; income is the fruit grown thereon, when it is severed, derived, therefrom. It is "ab extra." Before it matures, it is non-existent, as a thing separate from the capital. It is not severable until it matures, because it depends upon the capital to mature. The essential of a gift is delivery. In order to make a gift, **"the property must be in esse at the time of the donation"** (28 C. J. 644). One cannot make a gift of the unborn child of a slave or of an unborn calf or a crop not grown. **A gift of a thing not in being does not take effect until the thing comes into being.** (Note 7, 28 C. J. 644.) If the thing must ripen on the tree, it cannot be delivered apart from the tree until ripe.

So a gift of interest upon bonds, the bonds being retained, does not take effect until the interest becomes owing by the obligor. A gift of trust **income** does not take effect until the trust income comes into the trust. A gift of commissions, to accrue under an insurance agent's contract, does not take effect until the commissions come into being and become owing. **Delivery is not—cannot be—made before then.** At the time such income comes into existence, so that it can be severed and delivered—when the gift takes effect—the **owner** of the capital

receives it in the sense that it is then owing to and receivable by him. **The gift does not take effect until the income has come in, been realized, by the owner of the property.**

In *Rose v. Commissioner*, 65 F. (2d) 616, the Court evidently made a similar analysis. It said:

> "It is settled that assignment of a bare right to income will not relieve the assignor of tax liability thereon. Lucas v. Earl, 281 U. S. 111, 50 S. Ct. 241, 74 L. Ed. 731. This is on the ground that the income is the property of the assignor before any right thereto vests in the assignee. * * *"

This principle underlies and justifies the Supreme Court's statement that the power to give income is equivalent to the enjoyment of it; that is, there is no power to give it, to make delivery of it, essential to a gift, until it has become owing and become income to the owner of the property upon which the income grew and to which it adheres until it matures.

The principle underlying the Supreme Court's statement in the *Horst* case, quoted by the Court of Appeals in the case at bar, has no application to this case. Petitioner, after the assignment of this property to the trustee, was not the owner of the property. He did not own the tree upon which the fruit grew. In *Pearce v. Commissioner*, 315 U. S. 343, the Court, in the case of a grantor in trust, states that the principle of the *Horst* and similar cases is not applicable for the foregoing reason. The Court says (l. c. 353):

> "* * * in those cases the donor or grantor had 'parted with no substantial interest in property other than the specified payments of income.' Id. (312 U. S., p. 583, 85 L. Ed. 1058, 61 S. Ct. 759). Here he has parted with the corpus. * * *"

In the *Horst*, *Eubank*, and *Schaffner* cases, there was no question as to who owned the property. The only question was who realized the income, **qua income**, and it was ruled that the owner of the property, by virtue of its ownership, realized the income—that it came in to him before his gift took effect. In those cases, ownership of the income is found from admitted ownership of the property from which the income arose. The Court of Appeals applied the statement in the *Horst* case to the case at bar, as a premise to find ownership of the property from power over the income. **That is reasoning in reverse** and a *non sequitur*. Because the owner of property cannot give the income away without first receiving such income, it does not follow that power to give income away makes one the owner of property. A proper conclusion from established facts is not a premise to prove the existence of the facts necessary to establish the conclusion.

In *Helvering v. Stuart*, 317 U. S. 154, this Court said those cases were not controlling in a trust case **because in those cases there was no real disposition of the res by the grantor.**

The *Horst* and similar cases are not authority to find ownership of property in the settlor of a trust because of a power, not to receive, but to designate who, other than himself, shall receive income or corpus.

This Court's Decisions Concerning Transfer Taxes (e. g., Gift and Estate Taxes) Are Inapplicable to This Question Involving Income Taxes.

The taxable incident of **transfer taxes** (Estate Taxes and Gift Taxes) is the transfer of property. For such taxes, the possession of the right to transfer property is equivalent to the ownership of such property, because the only element of ownership of property upon which those taxes are imposed is the power to transfer. The other elements of ownership are immaterial.

In the case of the Gift Tax, beneficiaries of a trust—not the trustee—are the donees (*Helvering v. Hutchings*, 312 U. S. 393). For that reason, if a grantor in trust retains power to change the beneficiaries, he has retained power to make a gift and has not yet made a gift. That is the crux of *Sanford's Estate v. Commissioner*, 308 U. S. 39. In the case of the Estate Tax, transfer by death is the subject of the tax, so that, if the grantor at the date of death possessed the power to designate new beneficiaries, he has that element of ownership—the ability to transfer—which is the subject of the tax. That is the crux of such cases as *Chase National Bank v. U. S.*, 278 U. S. 327, and *Porter v. Commissioner*, 288 U. S. 436.

To the contrary, in the case of **income taxes**, the taxable element of the ownership of property is not the right to transfer it. The tax is upon income and the taxpayer is the person who receives the income or the economic benefit of it. The taxable element of ownership is the right to receive the income. Where the property has been transferred in trust, the question in the case of income taxes is not whether the beneficiaries of the trust have an indefeasible title or whether the grantor has the power to transfer it, **but whether the grantor after transfer to the trustees has retained such title that he receives or may receive the benefit of the income therefrom.**

Petitioner Is Not Liable for Income Tax Because His Retained Power Is Not Such That He Enjoyed or Could Enjoy the Economic Benefit of the Income.

In this case (except as to the income from which the alleged deficiency results) petitioner could change the beneficiaries of the income and the corpus and accelerate distribution of the corpus. He could not make any change under which he himself could receive anything or any economic benefit. His situation in life was such that there

was no person in being, or probably ever to come in being, who would be an intimate member of his family, whose enrichment might be of some economic benefit to him.

The trust was real. The title of the trustees was complete and indefeasible. Petitioner dispossessed himself of all title. The trust was not, as in the *Clifford* case, a mere reallocation of income in an intimate family group. Petitioner was poorer after the transfer in trust than before.

The essential equivalent of ownership of property, economic benefit, was not present. Ownership of property includes the right to keep and spend the income therefrom for the owner's personal use, support, or pleasure. The owner can rely upon the income and the principal as an assurance against future personal want or need. He can handle, possess, and use the corpus and income for his personal aggrandizement and gratification. None of these first and supreme economic contents of ownership is included in the power to appoint properties or income to others. Absent retention of such ownership the trust may not be disregarded **for Income Tax.**

The **grantor** of property in trust, who retains the power to appoint the property or the income therefrom to beneficiaries other than himself, can obtain no more benefit of the income from such property and no more benefit of the corpus than can the **donee** of such a power, that is, a person upon whom such a power is conferred by another. It is plain that a donee's economic benefit, from the income and from the property subject to his power, is just as great as that of the grantor. Although the donee of such a power, like the grantor retaining the power, is subject to the Estate and Gift Tax upon the exercise of his power, it is not contended that a donee of such a power is subject to Income Tax upon the income from the property subject to his power.

The decision of the Court in this case goes far beyond any other decision. In *Commissioner v. Buck,* 120 F. (2d) 775, the Court says:

> "We can best approach the instant case by enumerating the significant factors to be considered: That the donees are members of the donor's family, of which he is the head; that he has 'income in excess of normal needs'; that, during his life, he is unrestricted as to the disposition of any part of the corpus or income, excepting that he may not divert any portion for his personal use; that, while he lives, he has entire control of the management of the corpus, and, at his pleasure, may remove the trustee and appoint another."

Admittedly, one can enjoy economic benefit from income paid to one's wife, with whom one lives. There is still economic truth in the common law fiction that husband and wife are one. One may derive economic benefit from payment of income to any intimate member of his family—persons with whom one lives in a common home. But the income of matured sons and daughters, twenty-nine to fifty years of age, married and living apart, supporting themselves, affords no economic benefit to their father. Their security, ample income to them, may afford him personal pleasure and satisfaction, but it is not economically beneficial.

Only one of the three factors, which the Court emphasizes in the *Buck* case as the basis of its conclusion, is partially present in the instant case. There, as here, the donor was unrestricted as to the disposition of the corpus and unaccrued income except that he could not divert it to himself. The other factors are not present in the case at bar.

In *Helvering v. Clifford,* 309 U. S. 331, (1) the trust was for a short term, and then (2) the property held in trust (including capital gain received during the period of the

trust and enhancement in value of the property) reverted to the grantor, and (3) the grantor retained full administrative control over the property during the trust term, and (4) the income during the term was paid to grantor's wife or set aside, in his discretion, for her benefit. It was ruled that the trust constituted a mere reallocation of income in the intimate family group and that the grantor could not feel poorer after the trust. As the Board of Tax Appeals said in the *Clifford* case (Memo. Op. Docket 89,054, Sept. 26, 1938), the trust was without substance. The trustee in that case was merely the nominee of the grantor to receive the income in his behalf and then set it aside for his wife. Clifford was the owner of the trust property.

In *Helvering v. Stuart*, supra, this Court said:

> * * * "Economic gain realized or realizable by the taxpayer is necessary to produce a taxable income under our statutory scheme."

The opinion of The Tax Court of the United States, when the *John Stuart* case came back to it under this Court's mandate, is enlightening (2 T. C. 1103). It will be remembered that the grantor's wife and brother were the trustees, that the deficiencies were for the years 1934 and 1935, and that as to those years paragraph "Ninth" of the trust authorized the trustees, brother and sister of the grantor or the survivor of them, to change the beneficiary, among other powers of alteration. The Tax Court then found that:

> "Petitioner appointed his wife and his brother as trustees because he knew that they shared his point of view in regard to the children, their needs, and the purposes of the trusts, etc."

The Tax Court distinguished the *John Stuart* case from the *Clifford* case as follows:

> "There, the corpus of the trust was to revert to the grantor on its termination; here, petitioner could never receive the economic enjoyment of either the corpus or its income. There, the trust was for the benefit of the wife living in the same household with the grantor; here, the trusts were for adult children, two of whom had established separate residences from petitioner."

The trust at bar is not distinguishable from the *John Stuart* trust. Any factual difference is immaterial. The grantor retains as much power when he confers a general power to change beneficiaries, excluding himself as beneficiary, upon his wife and brother, who are familiar with and who will carry out his desires and purposes, as when he retains the power in himself. Both ways effectuate his desires and purposes. Taxes are practical. Technical rules of property do not conclude against the truth. This Court's decision in the *Stuart* case, as construed by The Tax Court, is on all fours with this case and should have concluded this case. The Court of Appeals' ruling is in conflict with this Court's decision in the *John Stuart* case.

The Court of Appeals' Decision Is Contrary to the Revenue Act.

Section 161 (b), Revenue Act 1938, concerning the tax upon estates and trusts, reads as follows:

> "The tax shall be computed upon the net income of the estate or trust, and shall be paid by the fiduciary, except as provided in section 166 (relating to revocable trusts) and section 167 (relating to income for benefit of the grantor)."

Section 162, Act of 1938, directs that certain income distributable to the beneficiaries shall be deductible in calculating the income of the trust and shall be included in the income of the beneficiary.

The foregoing is the general rule, and the quoted words direct that this general rule is subject to only two exceptions, set out in Sections 166 and 167.

In the *Clifford* case, the Board of Tax Appeals (Memo. Opinion, Docket No. 89,054, Sept. 26, 1938), held the trust not a real trust—that by the conveyance in trust the grantor did not dispossess himself of title and that the arrangement was an ineffectual attempt to secure a result whereby the fruits are attributed to a different tree from that on which they grew. This Court, in the *Clifford* case, held that although Clifford established a trust, it was without substance and therefore **not a real trust.** This is a sound **basis** for not applying the statutory direction concerning trusts. **When the trust is not a trust, it should not be treated as such.** When the conveyance is irrevocable and beyond recall, and the grantor dispossesses himself of all title to, and all benefit from, the property and vests it irrevocably in the trustee, then it is a real trust. *Seymour v. Freer*, 75 U. S. (8 Wall.) 202.

Sections 161 to 167, inclusive, I. R. C., are a code directing the manner of taxation and the persons to whom its income should be taxed **when the trust is real.**

Sections 161 to 165, inclusive, I. R. C., provide the general rule. Sections 166 and 167 are the exceptions. Sections 166 and 167 deal with powers of the grantor of the trust which shall make the income of the trust includable in his income. Section 166 covers trusts where the grantor or a person without adverse interest has power to revoke the trust and to revest title to the corpus of the trust in the grantor. Section 167 covers trusts where the grantor has discretion to distribute income to himself or to accumulate it for future distribution to him or to use the income for the payment of premiums on policies of insurance on his own life. Every exception is limited to a trust under which the grantor retains the **full** economic benefit of the trust estate.

When Congress so carefully limits every provision for taxation of the income of a trust to the grantor—to cases where the grantor's powers bring him an economic interest in the trust property or income, it has established the minimum, essential to taxation. Lesser powers than those enumerated in Sections 166 and 167, I. R. C., powers, under which no economic interest can be obtained by the grantor, cannot have this effect when Congress conditioned the larger powers upon the retention of an economic interest. The large power of revocation is substantially equivalent to ownership, and the careful limitations of it (excluding its application where the power is conditioned upon the consent of a person with an adverse interest so that the grantor's power must be substantially untrammeled) discloses an intent of Congress to **exclude** from treatment like that under Sections 166 and 167 and **include** within Sections 161 and 162 trusts where the grantor can receive no economic benefit—trusts where grantor's power is merely a power to appoint to other persons the use and benefit of the property.

The decision of this Court in the *Clifford* case sustains this contention.

We submit that, properly construed, that case rules that trust income not paid to the settlor is nevertheless taxable to the settlor under Section 22 (a) where the trust is not real and without substance and does not sustain such a tax where the trust is real. This Court should clarify its position and should take jurisdiction of this case that that may be done.

II.

The Decision of the Court in the Case at Bar Is Directly in Conflict With the Decisions of the Second Circuit in Knapp v. Hoey, 104 F. (2d) 99; the First Circuit in Commissioner v. Bateman, 127 F. (2d) 266.

In *Knapp v. Hoey,* supra, grantor reserved the same powers as petitioner, except that petitioner's power did not extend to the controverted income, as stated under point III below. In *Commissioner v. Bateman,* supra, grantor's powers were the equivalent of petitioner's.

In those cases the grantor was held not taxable upon the income.

III.

The Power of the Settlor Did Not Exist During the Period When the Income in Question Was Derived and Could Never Affect the Right to Such Income.

The trust indenture provides that "The Grantor may * * * modify or alter this indenture, * * *: (A) By disposing of the income derived **after any such modification or alteration becomes effective** otherwise than as originally provided in this indenture, * * *," and further, that such modification or alteration "must be by instrument in writing duly executed by the Grantor and delivered to the Trustees **and shall become effective thirty (30) days next following the delivery of such instrument.**"

The income in question was derived within thirty days after the execution of the trust. Petitioner could not make any alteration effective during that period and no alteration effective thereafter could deprive the named beneficiaries of this income. The beneficiaries named in the trust received an indefeasible right to such income without any power in the grantor at any time to modify or alter or in any manner to change or affect such right. The grantor has no reversion. The trust property never

comes back to him. And as to the income in question, he had no power whatever even to direct its course.

For at least thirty days following the execution of the trust the beneficiaries of the trust had an indefeasible, equitable interest in the trust estate from which the income was derived (*Irwin v. Gavit*, 268 U. S. 161). The property never reverts to the settlor. His power to modify the trust does not extend to the term when the income in question was received or to the income derived during such term. His power is effectual only after such term and as to income thereafter derived.

This trust was a valid, subsisting, and binding trust, at least for the period when the grantor had no power to change it and as to income which he could never change. A trust for a short term has been held valid even where the grantor had a reversion after the end of the term. A reversion after a short term is a much more substantial reason for attributing income from property to a grantor than a power after the term to change the beneficiaries which cannot be exercised so that he derives any benefit. In the one case, the settlor gets all of the benefit after the term; in the other, he gets none.

The opinion of the Court of Appeals, like the opinion of The Tax Court, misstates this contention and does not address itself to it. It is in conflict with the many decisions holding short term trusts valid, even when the property reverts to grantor, to-wit, *Helvering v. Bok*, 132 F. (2d) 365 (CCA 3); *Commissioner v. Jonas*, 122 F. (2d) 169 (CCA 2); *Jones v. Norris*, 122 F. (2d) 6 (CCA 10); *Central National Bank of Cleveland v. Commissioner*, 141 F. (2d) 352 (CCA 6); *Dunlevy-Milbank*, 41 B. T. A. 1014.

IV.

The End Result of the Conflicting Constructions, by the Various Courts, of This Court's Decision in the Clifford Case Is Intolerable Confusion.

The lower courts have held (1) that the retention of administrative power over the trust corpora is the determinative factor, e. g., *Stockstrom v. Commissioner*, 3 T. C. 255, and *U. S. v. Anderson*, 132 F. (2d) 98, and (2) contra, that the retention of such control is not sufficient, e. g., *Commissioner v. Katz*, 139 F. (2d) 107; *Plimpton v. Commissioner*, 135 F. (2d) 482; and (3) that retained power to change the beneficiaries is determinative **if coupled with directed distribution in the family group and also with administrative control of the trust property**, e. g., *Commissioner v. Buck*, 120 F. (2d) 775, and (4) contra, in the case at bar, that retained power to change the beneficiaries was sufficient **without any intimate family group or retention of administrative control**, and (5) that a short term of the trust is determinative if there is a reversion, *Price v. Comissioner*, 132 F. (2d) 95; and (6) contra, that it is not (cases supra, point III). The Tax Court and the Courts of Appeal are all at variance with each other and admittedly without any certainty of any conclusion. See *Williamson v. Com.*, 132 F. (2d) 489; *Commissioner v. Katz*, 139 F. (2d) 107; *Suhr v. Commissioner*, 126 F. (2d) 283; *Armstrong v. Commissioner*, 143 F. (2d) 700, reversing the Tax Court. "The Tax Court at present is deep in conflict over governing criteria" (Harvard Law Review, July, 1944, p. 884, note 368).

Congress is also confused. In 1942 Congress amended Section 22 (b) (3) of the Revenue Act. Before amendment, it read as follows:

> "(b) **Exclusions from Gross Income.**—The following items shall not be included in gross income and shall be exempt from taxation under this title:
>
> * * * * * * *

"(3) The value of property acquired by gift, bequest, devise, or inheritance (but the income from such property shall be included in gross income)."

The words in parentheses were the expression of the rule of *Irwin v. Gavit*, supra.

Sec. 111, Revenue Act 1942, amended paragraph (3) quoted above, so that the comparative part reads as follows:

"(3) The value of property acquired by gift, bequest, devise, or inheritance. There shall not be excluded from gross income under this paragraph, the income from such property, or in case the **gift,** bequest, devise, or inheritance **is of income from property,** the amount of such income." (Emphasis supplied.)

Notice the emphasized words. Income received by gift must be included in the income of the recipient. Income is income to only one person and cannot be income to both the donor and the donee.

It seems that Congress, in its apparent haziness, has changed the **salutary** rule of the *Horst, Eubank, Clifford, Schaffner* cases. One possible and even probable reason why Congress did this is this: The Commissioner of Internal Revenue and the Tax Court, in those trust cases in which the grantor retained some power either of administration or disposition of the trust property but no power to benefit from the trust, have ruled that the grantor was not only taxable on the income but also was subject to gift tax when such income was paid in accordance with the directions of the trust (*William Fleming*, 3 T. C. 974). This was confiscatory. Grantors were helpless. They could not escape from either tax.

This amendment, if our construction is right, is improvident and destructive of the tax. It resulted from this tumultuous snarl in the lower courts as to the taxation of trust income.

The further conflict with Congress, if the decision of the Court of Appeals in this case is allowed to stand, is made evident from consideration of Section 134, Revenue Act 1943, enacted February 25, 1944.

In the *Stuart* case, the Court held that income of a trust which, under its terms, may be distributed in the discretion of the grantor or the trustees (who have no adverse interest) for the maintenance of a beneficiary whom the grantor is legally obligated to support, is taxable to the grantor under Section 167, I. R. C. Said Section 134 changed this rule. It provides that:

> "(c) Income of a trust shall not be considered taxable to the grantor under subsection (a) **or any other provision of this chapter** merely because such income, in the discretion of another person, the trustee, **or the grantor acting as trustee** or cotrustee, may be applied or distributed for the support or maintenance of a beneficiary whom the grantor is legally obligated to support or maintain, **except to the extent that such** income is so applied or distributed."

Subsection (b) of Section 134 makes this provision retroactive if the parties interested consent thereto.

So, under said Section 134 and the Court of Appeals' decision in the case at bar, you have this anomalous situation: A reserved power of a grantor to give income to persons for whose support or maintenance he has no legal obligation makes the income taxable to him under Section 22 (a), I. R. C. But power of a grantor, as trustee, to do the same thing for the benefit of persons whom he is legally obligated to support does not have this result. In the case where the grantor might derive an economic benefit from the power, the income is not taxable to him, but in the case where he can derive no such economic benefit, it is. It is apparent that Congress did not construe the law as did the Court of Appeals in the instant case.

The lower tribunals attempt to "echo" this Court's decisions. Generally, they admit they have no settled confidence in their conclusions upon this question. *Williamson v. Commissioner,* 132 F. [2d] 489). The application of the statute, like a thread, becomes snarled worse, as each Inferior Court attempts to apply the rule of the *Clifford* case to new facts, without grasping the principle. This Court alone can settle this corroding controversy.

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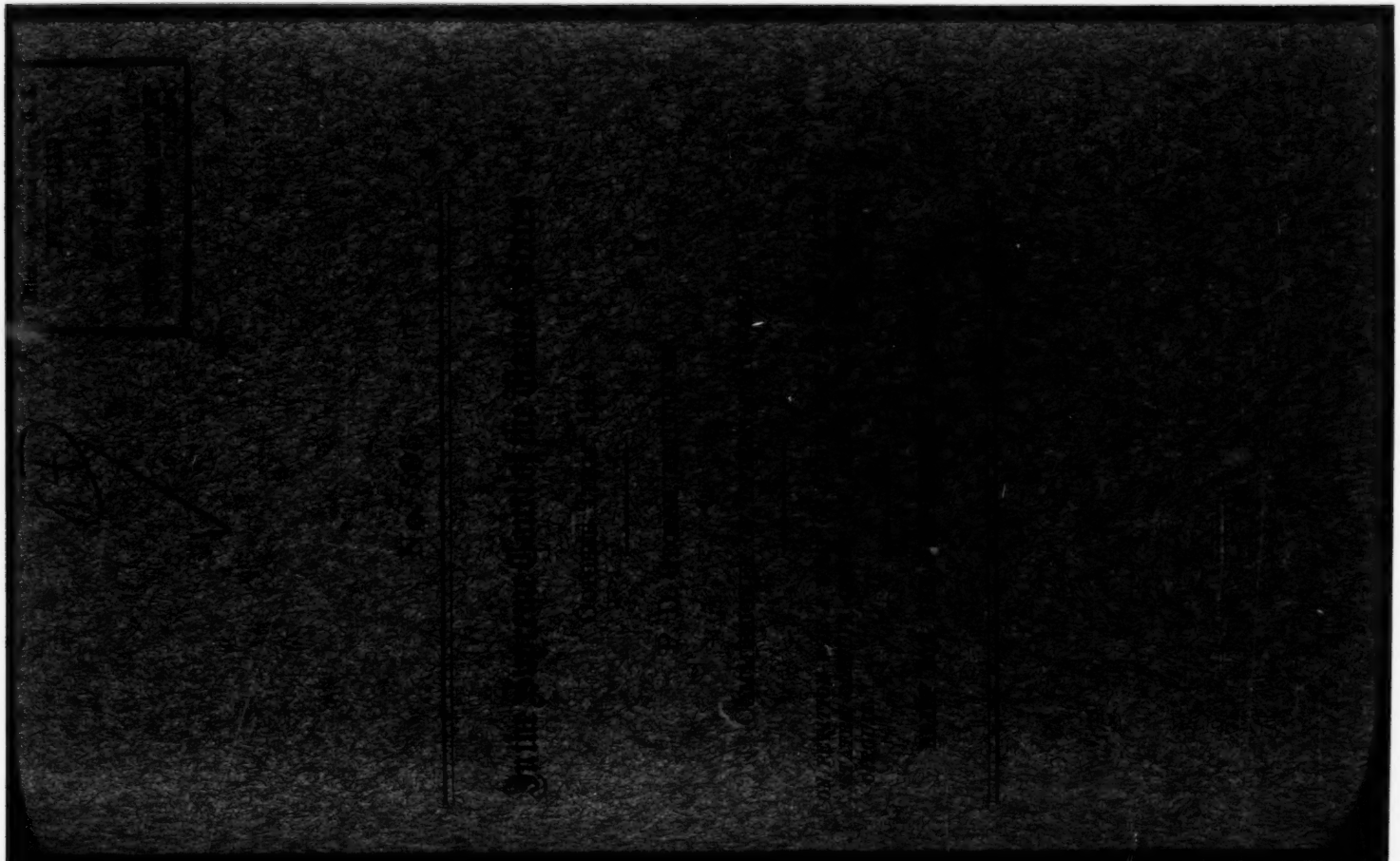

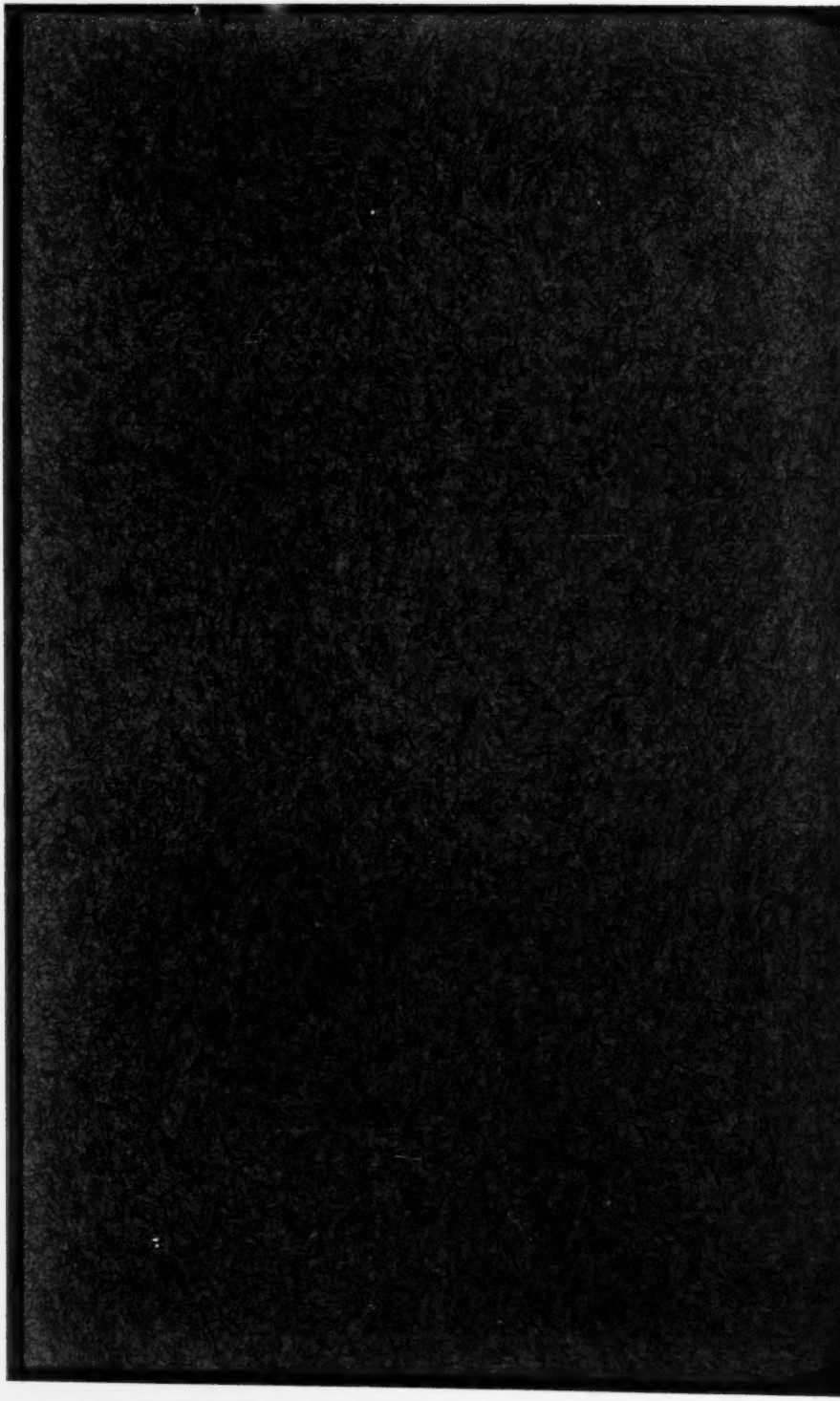

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In the Supreme Court of the United States

OCTOBER TERM, 1944

No. 595

P. D. GEORGE, PETITIONER

v.

COMMISSIONER OF INTERNAL REVENUE

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE EIGHTH CIRCUIT

BRIEF FOR THE RESPONDENT IN OPPOSITION

OPINIONS BELOW

The memorandum opinion of the Tax Court (R. 10–24) is unreported. The opinion of the circuit court of appeals (R. 44–53) is reported in 143 F. 2d 837.

JURISDICTION

The judgment of the circuit court of appeals was entered on July 17, 1944 (R. 54). The petition for a writ of certiorari was filed on October 13, 1944. The jurisdiction of this Court is invoked under Section 240 (a) of the Judicial Code, as amended by the Act of February 13, 1925.

QUESTION PRESENTED

Whether the grantor of a family trust, the corpus of which consists of shares of stock of a corporation which was managed and controlled by the grantor, is taxable on the income therefrom, under Section 22 (a) of the Internal Revenue Code where he names himself and two other individuals as trustees with broad powers of management, and reserves the power to change the shares of beneficial interest in the income and principal of the trust fund, although he cannot direct payment to himself or his estate.

STATUTE AND REGULATIONS INVOLVED

The statute and regulations involved are set out in the Appendix, *infra,* pp. 12–17.

STATEMENT

The Tax Court found the following facts (R. 11–15):

On December 23, 1939, the taxpayer created a trust naming himself and two other individuals as trustees. Neither of the other two trustees is related to the taxpayer. The taxpayer transferred 640 shares of the capital stock of the P. D. George Company to the trust. (R. 11.) Under the trust instrument the trustees are given broad powers of management. The trust instrument provides, *inter alia,* that the assets thereof are to be divided into seven parts. The income of the first of such parts is to be paid to one son, Pericles

F. George, in quarterly or other convenient installments for life, or in certain eventualities to his wife and children, and, on his death, the corpus is to be distributed to his then living children and to the descendants of any child then dead, per stirpes. The entire net income of the remaining six parts is to be paid to the six other sons equally, in quarterly or other convenient installments, until five years after the death of the taxpayer, at which time the corpus of those parts then remaining is to be distributed to the six sons or, in the event of the death of any of them before the period of termination, to his descendants, per stirpes. Article Three of the trust instrument provides, *inter alia,* that (R. 35–36)—

> In the event of the death of any of Grantor's seven (7) sons leaving no descendant then living, the share held for such son shall go to the others of Grantor's said seven (7) sons, and to the descendants then living, per stirpes, of any of them who have died, * * *
>
> * * * * *
>
> If all of Grantor's said six (6) sons and the said children of Pericles Francis George should die before their respective shares have been paid over to them, free from trust, and no descendant of any of them is living to take the trust estate, then upon the death of the last survivor of them and Pericles Francis George, the trust estate shall be paid over and distributed to the

persons who may then be the heirs at law of the Grantor, according to the laws of the State of Missouri then in force.

Article Six of the trust instrument provides as follows (R. 36–38):

These trusts are created and the interests of the beneficiaries, hereinbefore set out, shall be vested, but subject however to divestiture as follows:

1. The Grantor may at any time and from time to time modify or alter this indenture and the disposition of the trust property and the estates and interests therein created and the income arising therefrom, but in the following particulars only:

(A) By disposing of the income derived after any such modification or alteration becomes effective otherwise than as originally provided in this indenture, or otherwise than as provided by any amendment, by altering the proportion or amount of such income to be paid to or applied to the use of any one or more of the beneficiaries, by cancelling the share of any one or more of the beneficiaries in whole or in part, by substituting any beneficiary or beneficiaries in the place of any one or more of them, by adding to the number of beneficiaries, by providing for the proportion or amount of income to be paid or applied to the use of such additional or substituted beneficiaries; provided, however, that in no event shall any such modification or alteration (one or

more) direct, permit or allow the said income to be accumulated for or paid or applied to or for the use or benefit of the Grantor.

(B) By directing the distribution of the principal of any of the trust estates, as the same shall be constituted at any time, otherwise than as originally provided in this indenture, or otherwise than as provided by any amendment, by altering the proportion or the amount of the principal of any of the trust estates to be assigned, paid, and set over to any one or more of the beneficiaries, by cancelling the share of any one or more of the beneficiaries in whole or in part, by substituting any beneficiary or beneficiaries in the place of any one or more of them, by adding to the number of said beneficiaries, by providing for the proportion or amount of the principal of any of the trust estates to be assigned, paid, and set over to such additional or substituted beneficiary, or for the manner in which all or any part of said principal shall be divided or distributed upon the termination of the trusts; provided, however, that in no event shall any such modification or alteration direct, permit or allow any part of the principal of the trust estates to be paid or applied to or for the use or benefit of the Grantor or his estate.

(C) Any modification or alteration of this indenture provided for in subdivisions (A) or (B) of this Article Six must be by instrument in writing duly executed by the

> Grantor and delivered to the Trustees and shall become effective thirty (30) days next following the delivery of such instrument.
>
> 2. The Grantor may at any time and from time to time direct the Trustees to distribute, free from trust, any share of a beneficiary, in whole or in part, to the beneficiary who shall be then entitled to the income currently distributable therefrom; provided, however, that any such direction must be by instrument in writing duly executed by the Grantor and delivered to the Trustees, and shall become effective on the delivery of such instrument, and the Trustees shall immediately make distribution as in such instrument directed.

The trust instrument provides further that while the taxpayer is serving as a co-trustee he is to receive one-half of the compensation to be paid to the trustees for their services rendered to the trust; the other half is to be divided equally between the other trustees. The taxpayer has never exercised his power under the above-quoted Article Six to change the interests of the beneficiaries. (R. 13.)

During the taxable year, the youngest of the taxpayer's sons was 29 years of age and the oldest was 43 years of age. For many years prior to December, 1939, and continuously since that time, the seven sons have been married and living apart from the taxpayer and apart from each other. During 1939, and for many years prior thereto,

each of the seven sons had an independent income, in addition to his share of the trust income in 1939, and maintained himself and his family. The trustees adopted the calendar year as the accounting period of the trust and reported the income of the trust for each calendar year ending December 31. (R. 13–14.)

During 1939, prior to the creation of the trust for the benefit of the taxpayer's sons, the taxpayer owned all of the 1,000 shares of the P. D. George Company. The stock then had a value of $700 a share. In addition to the transfer of the 640 shares to the trust for the benefit of his sons, the taxpayer transferred 60 shares of such stock by gift on December 23, 1939. At no time during 1939 did the taxpayer own assets in excess of $50,000, except for the stock in the P. D. George Company. The income tax return of taxpayer for the taxable year shows that he received $15,000 as salary from the P. D. George Company; dividends in the amount of $38,519.38, including dividends from the P. D. George Company of $36,000; interest in the amount of $647.23; $960 as trustee's fee in the P. D. George trust; and that his net income was $49,896.89. (R. 14.)

Between December 23, 1939, when the trust was created, and December 31, 1939, the gross income received by the trustees amounted to $76,800, all of which was distributed before December 31, 1939. Of this amount $74,880 was

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distributed to the seven sons and $1,920 to the trustees for services as provided under the terms of the trust instrument. On his federal income tax for 1939, the taxpayer reported in his gross income his share ($960) of trustees' commissions, but did not report any other part of the $76,800. The Commissioner denied the total trustees' commissions as a deduction from the income of this trust and increased the taxpayer's income by the total amount of the gross income of the trust on the ground that such amount was taxable to the taxpayer under Section 22 (a) of the Internal Revenue Code. In the Tax Court, it was stipulated that the amount of such increase was excessive by the amount of $960. (R. 14–15.)

The Tax Court found (R. 17) that the taxpayer "retained an interest in the corpus of that trust [for his sons] substantially equivalent to continuing ownership thereof", and held that the Commissioner did not err in including in taxpayer's income the $75,840 (R. 18). The court below affirmed (R. 53).

ARGUMENT

Both the Tax Court and the court below held that the taxpayer remained in substance the owner of the trust funds within the meaning of *Helvering* v. *Clifford,* 309 U. S. 331, and we submit that there can be little doubt as to the correctness of such holding. It is in line with decisions in the

Second and Third Circuits (*Commissioner* v. *Buck,* 120 F. 2d 775 (C. C. A. 2d); *Hyman* v. *Nunan,* 143 F. 2d 425 (C. C. A. 2d); *Brown* v. *Commissioner,* 131 F. 2d 640 (C. C. A. 3d), certiorari denied, 318 U. S. 767; *Foerderer* v. *Commissioner,* 141 F. 2d 53 (C. C. A. 3d)) and is not in conflict with any decision of this Court or any circuit court of appeals.

In support of the application for certiorari, the taxpayer asserts a conflict with numerous cases (Pet. 6–7), apparently placing his chief reliance upon *Knapp* v. *Hoey,* 104 F. 2d 99 (C. C. A. 2d); *Commissioner* v. *Buck, supra;* and *Commissioner* v. *Bateman,* 127 F. 2d 266 (C. C. A. 1st). True, *Knapp* v. *Hoey* held the grantor not accountable for the trust income even though he had retained the power to shift shares of beneficial interest in the trust. But the decision was grounded upon Section 166 of the Revenue Acts of 1928 and 1932, relating to revocable trusts; it antedated the *Clifford* case and the Government did not assert taxability under Section 22 (a). In a later case in the same circuit, *Commissioner* v. *Buck, supra,* the court followed *Knapp* v. *Hoey* with respect to Section 166 but took the view (p. 778) that it was of no assistance in construing Section 22 (a), and held the grantor accountable under that Section in the light of the *Clifford* case. Since the *Buck* case was decided in the Commissioner's favor, it is diffi-

cult to understand the contention of the taxpayer here that it conflicts with the decision below. The *Bateman* case was decided in favor of the taxpayer; but there the grantor did not retain as much control over the trust property as retained by the grantor herein or by Buck in his case; and, indeed, the court in the *Bateman* case expressly distinguished the *Buck* case, saying (p. 270), that it was "an easy case for applying the *Clifford* principle".

The taxpayer also urges that during the tax year in question (1939) he had no power to control the disposition of the income because the trust was created on December 23, 1939, and he was required, under the terms of the trust instrument, to give 30 days' notice if he wished to exercise his power to change the beneficiaries. But since the taxpayer was the owner of the corpus, this argument has no vitality under the *Clifford* rule, and both the Tax Court (R. 19–20) and the court below (R. 53) so held. There is nothing in *Helvering* v. *Stuart,* 317 U. S. 154, to cast any doubt on the ruling below, for the *Stuart* case is in no way a departure from the rule of the *Clifford* case and other similar cases (*Helvering* v. *Horst,* 311 U. S. 112; *Helvering* v. *Eubank,* 311 U. S. 122; *Harrison* v. *Schaffner,* 312 U. S. 579).

Finally, we submit that the instant situation comes within the scope of *Dobson* v. *Commissioner,* 320 U. S. 489, 501, rehearing denied, 321

U. S. 231, and since it cannot be said that the decision of the Tax Court is without warrant in the record or that it lacks an adequate basis in the law, the decision must stand. The court below upheld this view (R. 53).

CONCLUSION

The decision is correct; there is no conflict; the petition should be denied.

Respectfully submitted.

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APPENDIX

Internal Revenue Code:

> SEC. 22. GROSS INCOME.
>
> (a) *General Definition.*—"Gross income" includes gains, profits, and income derived from salaries, wages, or compensation for personal service, of whatever kind and in whatever form paid, or from professions, vocations, trades, businesses, commerce, or sales, or dealings in property, whether real or personal, growing out of the ownership or use of or interest in such property; also from interest, rent, dividends, securities, or the transaction of any business carried on for gain or profit, or gains or profits and income derived from any source whatever. * * *
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> * * * * *
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> (26 U. S. C. 22.)

Treasury Regulations 103, promulgated under the Internal Revenue Code:

> SEC. 19.22 (a)–1. *What included in gross income.*—Gross income includes in general compensation for personal and professional services, business income, profits from sales of and dealings in property, interest, rent, dividends, and gains, profits, and income derived from any source whatever, unless exempt from tax by law. (See sections 22 (b) and 116.) In general, income is the gain derived from capital, from labor, or from both combined, provided it be understood to include profit gained through a sale or conversion of capital assets. * * *
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> * * * * *

SEC. 19.166–1 [as amended by T. D. 5194, 1942–2 Cum. Bull. 53, 62]. *Trusts with respect to the corpus of which the grantor is regarded as remaining in substance the owner.*—(*a*) *Scope.*—If the grantor of a trust is regarded, within the meaning of the Internal Revenue Code, as remaining in substance the owner of the corpus thereof, the income therefrom is not taxable in accordance with the provisions of sections 161, 162, and 163 but remains attributable and taxable to the grantor, except as provided in section 22 (k) and section 171. This section deals with the taxation of such income. As used in this section, the term "corpus" means any part or the whole of the property, real or personal, constituting the subject matter of the trust.

(*b*) *Test of taxability to grantor.*—Section 166 defines with particularity instances in which the grantor is regarded as in substance the owner of the corpus by reason of the fact that he has retained power to revest the corpus in himself. For the purposes of this section the grantor is deemed to have retained such power if he, or any person not having a substantial interest in the corpus or the income therefrom adverse to the grantor, or both, may cause the title to the corpus to revest in the grantor. A bare legal interest, such as that of a trustee, is never substantial and never adverse. If the title to the corpus will revest in the grantor upon the exercise of such power, the income of the trust is attributed and taxable to the grantor (except as provided in section 22 (k) or section 171) regardless of—

(1) whether such power or ability to retake the trust corpus to the grantor's own

use is effected by means of a power to revoke, to terminate, to alter or amend, or to appoint;

(2) whether the exercise of such power is conditioned on the precedent giving of notice, or on the elapsing of a period of years, or on the happening of a specified event;

(3) the time at which the title to the corpus will revest in the grantor in possession and enjoyment, whether such time is within the taxable year or not, or whether such time be fixed, determinable, or certain to come;

(4) whether the power to revest in the grantor title to the corpus is in the grantor, or in any person not having a substantial interest in the corpus or income therefrom adverse to the grantor, or in both;

(5) when the trust was created.

But the provisions of section 166 are not to be regarded as excluding from taxation to the grantor the income of other trusts, not specified therein, in which the grantor is, for the purposes of the Internal Revenue Code, similarly regarded as remaining in substance the owner of the corpus. The grantor is regarded as in substance the owner of the corpus, if, in view of the essential nature and purpose of the trust, it is apparent that the grantor has failed to part permanently and definitively with the substantial incidents of ownership in the corpus.

In determining whether the grantor is in substance the owner of the corpus, the Internal Revenue Code has its own standard, which is a substantial one, dependent neither on the niceties of the particular conveyancing device used nor on the tech-

nical description which the law of property gives to the estate or interest transferred to the trustees or beneficiaries of the trust. In that determination, among the material factors are: The fact that the corpus is to be returned to the grantor after a specific term; the fact that the corpus is or may be administered in the interest of the grantor; the fact that the anticipated income is being appropriated in advance for the customary expenditures of the grantor or those which he would ordinarily and naturally make; and any other circumstance bearing on the impermanence and indefiniteness with which the grantor has parted with the substantial incidents of ownership in the corpus.

Thus, the grantor is regarded as being in substance the owner of the corpus if, in any case, the trust amounts to no more than an arrangement whereby the grantor, in the ordering of his affairs, finds it expedient to entrust for a period the title to, and custody or management of, certain of his property to a trustee, the income from such property to be used by the trustee during such period to make those expenditures which the grantor would customarily or ordinarily or naturally make and to which the grantor chooses to commit himself in advance, while the corpus is to be held intact, for return in due course to the grantor. In such a case, it is immaterial that, at the time of the creation of the trust, an irrevocable disposition or consummated gift was made of those property rights which consist of the right to the expected future income of the corpus for the specified period. On the other hand, if the grantor, incident to a definitive and

permanent disposition of certain of his property, creates the trust in order to conserve the property, not for himself but for the donees, who will ultimately enjoy it, the provisions of sections 161, 162, and 163 are applicable.

For example, a grantor is regarded as remaining in substance the owner of the corpus of the trust, if he has placed it in trust for his son, John,

(A) for the term of three years, at the end of which time the trust might be extended for a like period at the option of the grantor and successively thereafter, but in the absence of such an extension the title is once more to revest in the grantor in possession and enjoyment; or

(B) for the term of a year and a day, then to be distributed to whomsoever the wife of the grantor shall by deed appoint (the wife not having a substantial adverse interest in the disposition of the corpus or the income therefrom); or

(C) for the term of the grantor's life, then to be distributed to John, the grantor reserving, however, the right to alter, amend, or revoke any provision of the trust instrument, upon notice of a year and a day.

In these typical cases the grantor is regarded as having retained the substantial incidents of ownership with respect to the income-producing property since the corpus will or may once more revest in himself in (A) upon the expiration of the trust period if the grantor does not exercise his option to extend the trust, in (B) upon the designation of the grantor as distributee, by a person not substantially and adversely interested, and in (C) upon the revocation of

the trust instrument or an alteration or amendment thereof, resulting in the designation of the grantor as distributee.

If, however, the grantor strips himself of the substantial incidents or attributes of ownership in the corpus retained by him so that he ceases to be regarded as in substance the owner of the corpus, the income thereof realized after the effective date of such divesting is not taxable to the grantor but is taxable as provided in sections 161, 162, and 163.

A person may have an interest that is both substantial and adverse to the grantor in the disposition of only part of the corpus or the income therefrom. If the power to revest title in the grantor is vested in him in conjunction with such person, or is vested solely in such person, there is to be excluded in computing the net income of the grantor only the income of such part.

(*c*) *Income and deductions.*—If the grantor is regarded as remaining in substance the owner of the corpus, except as provided in sections 22 (k), 23 (u), and 171, the gross income of such corpus shall be included in the gross income of the grantor, and he shall be allowed those deductions with respect to the corpus as he would have been entitled to had the trust not been created.

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